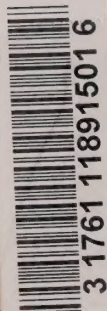


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Ontario Energy Board



IN THE MATTER OF THE
ONTARIO ENERGY BOARD ACT

AND

IN THE MATTER OF APPLICATIONS BY

THE CONSUMERS GAS COMPANY LTD.

**FOR ACQUISITION OF SHARES OF TECUMSEH GAS
STORAGE LIMITED AND RELATED ASSETS FROM
IMPERIAL OIL LIMITED**

E.B.O. 171

E.B.R.L.G. 35 - 5

**REPORT OF THE BOARD TO
THE LIEUTENANT GOVERNOR
IN COUNCIL**

Pour des renseignements en français, veuillez communiquer
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(La Commission accepte les appels
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Ontario Energy Board



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E.B.O. 171
E.B.R.L.G. 35-5

IN THE MATTER OF the Ontario Energy Board Act, R.S.O.
1980, Chapter 332, as amended;

AND IN THE MATTER OF an Application by The
Consumers' Gas Company Ltd. for leave of the Lieutenant
Governor in Council to acquire more than 20 percent of the
shares of Tecumseh Gas Storage Limited from Imperial Oil
Limited.

AND IN THE MATTER OF an Application by Tecumseh
Gas Storage Limited for the leave of the Lieutenant Governor
in Council to permit the sale, lease, conveyance or disposition
of its gas storage system to The Consumers' Gas Company
Ltd.

AND IN THE MATTER OF an Application by The
Consumers' Gas Company Ltd. and Tecumseh Gas Storage
Limited for the leave of the Lieutenant Governor in Council
to amalgamate.

AND IN THE MATTER OF an Application by The
Consumers' Gas Company Ltd. for approval of the Ontario
Energy Board with respect to certain undertakings given by
The Consumers' Gas Company Ltd.

BEFORE: P.W. Chapple
Presiding Member

C.A. Wolf Jr.
Member

R.R. Perdue
Member

REPORT OF THE BOARD

December 10, 1991

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1. INTRODUCTION

1.1 THE AGREEMENT

1.1.1 On December 28, 1990 The Consumers' Gas Company Ltd. ("Consumers") entered into an agreement ("the Agreement") with Imperial Oil Limited ("Imperial") to purchase from Imperial its shares of Tecumseh Gas Storage Limited ("the Shares"), ("Tecumseh").

1.1.2 In addition to the purchase of the Shares, the Agreement requires Consumers to purchase certain other business assets of Imperial ("the Assets") which are not regulated by the Ontario Energy Board ("the Board").

1.2 THE APPLICATIONS

1.2.1 On February 7, 1991 Consumers filed an application with the Board pursuant to Section 26 of the Ontario Energy Board Act ("the Act") for leave of the Lieutenant Governor in Council ("the LGIC") to allow Consumers to acquire the Shares.

1.2.2 On the same date, application was also made for leave of the LGIC to allow Consumers to purchase the Assets. The purchase of the Assets requires leave of the LGIC pursuant to certain undertakings dated

December 13, 1990 ("the Undertakings") which Consumers, amongst others, gave to the LGIC as a result of the LGIC's granting consent for British Gas plc to purchase most of Consumers' common shares. Article 4.2 of the Undertakings obligates Consumers to seek the approval of the LGIC to purchase any assets which are not regulated by the Board.

- 1.2.3 At the outset of the hearing on September 17, 1991 Consumers and Tecumseh withdrew two further applications which, if granted, would have permitted the two companies to amalgamate or, in the alternative, for Consumers to purchase all of Tecumseh's assets.

1.3 THE HEARING

- 1.3.1 On March 15, 1991 the Board issued a Notice of Application and on September 4, 1991 a Notice of Hearing setting September 17, 1991 as the date for the commencement of the hearing of the applications. The hearing commenced as scheduled and continued on September 19 at which time oral argument was heard.

- 1.3.2 A copy of the verbatim transcript of the proceedings and all exhibits are available for review in the Board's offices.

- 1.3.3 The Board has evaluated all the relevant evidence and submissions. However, it has chosen to summarize the evidence and positions of the parties only to the extent considered necessary or appropriate to deal with specific issues.

1.4 APPEARANCES

1.4.1 The following is a list of participants in the hearing and their representatives:

Consumers	Peter Atkinson
Board Staff	John Campion
Union Gas Limited	Michael Verwegen
Centra Gas Ontario Inc.	Paul Tolton

1.5 WITNESSES

1.5.1 The following witnesses appeared on behalf of Consumers:

F. James Tricker	General Manager, Tecumseh
Rudolf G. Riedl	Vice-President, Gas Supply, Consumers
Ronald S. Lougheed	Senior Vice-President Gas Supply, (Retired) Consumers
John L. Aiken	Senior Vice-President and Chief Financial Officer, Consumers

REPORT OF THE BOARD

2. BACKGROUND AND POSITIONS OF THE PARTIES

2.1 BACKGROUND

2.1.1 Tecumseh was formed in 1963 by Imperial and Consumers as a natural gas storage company with each of the parties holding 300,000 common shares of Tecumseh and having the right to nominate three directors to Tecumseh's board of directors. No other Tecumseh shares are issued and outstanding.

2.1.2 Tecumseh's storage operations commenced in 1964 in three reservoirs, Corunna, Seckerton, and Kimball-Colinville. Since that time two additional reservoirs have been acquired, Wilkesport and Dow Moore.

2.1.3 Tecumseh's annual turnover volume of gas (the total injected and withdrawn from storage) has increased from 7 Bcf in 1964 to 77.5 Bcf. Gas delivered from Tecumseh has represented approximately one-quarter of Consumers' annual sales volume during the winter months and almost half of Consumers requirements on peak days.

2.1.4 In late 1989 and early 1990 Consumers and Imperial informally discussed the possibility of Consumers purchasing the Shares. Consumers subsequently learned that Imperial was interested in selling all of its downstream assets located in Ontario which included both the Assets and

the Shares. On September 14, 1990 Consumers offered Imperial \$19.6 million for the Shares only. The book value of the Shares at that time was \$15.3 million.

2.1.5 Imperial did not respond to that offer and it expired on October 5, 1990. However, it then notified Consumers that it would sell the Shares at the offered price but only as part of a package which would also include the Assets.

2.1.6 Subsequently Consumers entered into the Agreement with Imperial.

2.1.7 The Agreement provides that Consumers would acquire certain of the Assets directly from Imperial and certain others indirectly through the purchase of all of the issued and outstanding shares of 923726 Ontario Limited.

2.1.8 In addition to the shares of 923726 Ontario Limited, the Assets consist of the following:

- petroleum and natural gas leases which contain the right to produce original gas in the Kimball-Colinville, Corunna and Seckerton pools and 14.7 Bcf of native gas in these pools which has been used by Tecumseh as cushion gas;
- the crude oil facilities in the Corunna and Seckerton pools and a four inch pipeline running from the pools to the Marcus crude oil terminal in Sarnia and;
- the petroleum and natural gas leases, storage leases, certain interests and facilities relating to the Ladysmith Pool;

certain protective storage leases, miscellaneous petroleum and natural gas rights, gross overriding royalties and other tangibles.

- 2.1.9 The Agreement was made conditional upon Consumers obtaining the necessary approvals of the LGIC, the Board and Investment Canada. Consumers testified that it anticipated that an agreement would be reached with Imperial to extend the closing date from September 30, 1991 to December 31, 1991.
- 2.1.10 Pursuant to the Agreement the price to be paid by Consumers for the Shares is \$19.6 million and for the Assets is \$13.9 million.
- 2.1.11 The Agreement provides that Tecumseh will assume liability for all environmental damage attributable to the properties which form part of the Assets.
- 2.1.12 After the signing of the Agreement it was decided that Tecumseh would pay a dividend in the aggregate amount of \$240,000. Therefore, on February 28, 1991 the Agreement was amended to adjust the purchase price by the amount of the dividend.
- 2.1.13 Also, after the signing of the Agreement, the Board issued its Decision in E.B.R.O. 466, the Tecumseh rates case, in which the Board directed Tecumseh to write down its rate base by approximately \$2.9 million, the cost of which was to be borne by Tecumseh's shareholders. Mr. Aiken testified that the potential of such a write-down was taken into account during negotiations even though the E.B.R.O. 466 Decision was not known at the time.

2.2 APPLICANT'S POSITION

- 2.2.1 It was Consumers' testimony that Imperial had stated that it was not interested in any further expansion of Tecumseh and its storage facilities. Consumers wished to gain control of Tecumseh in order to be in a position to expand the storage facilities to meet the needs of its customers. It was concerned that if Imperial sold the Shares to a third party a deadlocked board could result because of the arrangement whereby each 50 percent shareholder was entitled to elect an equal number of directors to the board of Tecumseh.
- 2.2.2 Witnesses for Consumers testified that the current contracted capacity of Tecumseh is 77.5 Bcf and that next year it has contracted to increase the capacity to 83.4 Bcf. Between 1991 and 2000 Consumers will require 15 to 20 more Bcf of storage. Consumers plans to develop the Ladysmith reservoir as a natural gas storage pool and it is anticipated it will provide an additional 3 Bcf of storage. Consumers is hopeful that it can be ready for injection by the summer of 1993. It is also planned to increase the pressure of the Dow Moore pool over its discovery pressure and thus increase its storage capacity which will add another 5.9 Bcf to the system.
- 2.2.3 With respect to the oil production assets, Consumers' witnesses testified that the recovery of oil from a producing reef was increased by virtue of the increased pressure normally undertaken when the reef was converted to a storage pool. They testified that while the oil assets were not essential to the gas storage operations, the public in general benefitted from the increased recovery of about 180,000 barrels of oil. It was Consumers' evidence that it did not intend to include these assets in either regulated business once the planned corporate reorganization was completed.
- 2.2.4 Consumers plans to finance the transaction through short-term debt and it has been informed by rating agencies that there will be no change in its credit rating as a result of the transaction.

- 2.2.5 Counsel for Consumers, Mr. Atkinson, argued that the primary purpose of Section 26(2) of the Act was to ensure a review of the suitability of an applicant and on that basis there could be no doubt that Consumers, Canada's largest natural gas distribution company and the holder of 50 percent of Tecumseh's shares since 1963, is a suitable applicant.
- 2.2.6 In addition, he argued that there were other public interest benefits to be considered and that they included the benefits to Consumers' customers particularly with respect to cost and security of supply.
- 2.2.7 He argued that any alternative to the development of Tecumseh's storage areas, such as obtaining storage in Michigan or expansion of the TransCanada PipeLines Ltd. ("TCPL") system would be more costly. He also pointed out that with the advent of deregulation in the natural gas industry, storage facilities enabled Consumers to purchase natural gas at lower spot prices in the summer and to give their customers the benefit of these prices in the winter.
- 2.2.8 With respect to security of supply, Counsel for Consumers argued that customers were entering into their own private arrangements for the supply of gas because of deregulation and as a result, the issue of backstopping had become more critical. With increased storage capacity, he said Consumers would be in a better position to provide this backstopping in the event of the failure of one of the private suppliers. He also argued that in the event of a breakdown on the TCPL system, storage would be available to provide back-up service.
- 2.2.9 Mr. Atkinson stated that Consumers was not seeking approval of the purchase price for the Shares or the Assets as that matter would be decided in an appropriate rates hearing. In any event he argued that the Board ought not to be concerned about the purchase price for the Shares or the Assets since Consumers had been closely involved with Tecumseh since its inception and therefore was very knowledgeable about the business. As

well, he argued that there was no doubt about Consumers' financial capacity to handle the transaction.

2.3 POSITION OF BOARD STAFF

2.3.1 Board Staff did not take issue with the suitability of Consumers as an acquirer of more than 20 percent of the shares of Tecumseh nor with the financial capacity of Consumers to conclude the transaction.

2.3.2 However, Counsel for Board Staff disagreed with Consumers' emphasis on the importance of storage and stated that rather, the focus ought to have been on whether additional storage would have been developed regardless of who owned the Shares. He argued that it was difficult to believe that additional storage would not have been developed in any event and that if a third party had purchased the Shares, Consumers' customers would have benefitted from increased storage without bearing the cost of the capital investment in the Shares.

2.3.3 Board Staff argued that subject to certain concerns which will be reviewed in a normal rates case, the transaction does not adversely affect the public interest. Those concerns were whether or not the investment represents a good use of Consumers' capital; the size of the capital investment; and inter-generational and inter-customer issues.

3. RECOMMENDATIONS OF THE BOARD

3.1 INTRODUCTION

3.1.1 Tecumseh is the latest of Ontario's major storage or distribution companies to undergo a significant change in its ownership.

3.1.2 Since 1985 the Board, in accordance with Section 26 of the Act, has held hearings and made recommendations in regard to the sale of each of the major gas distribution utilities in Ontario. As a result of these hearings the Board has accumulated a significant body of experience in evaluating transfers of ownership.

3.1.3 Generally speaking, the hearings produced a straight forward but nonetheless complicated question to be asked in each case: is the public interest being adversely affected by the proposed transaction?

3.1.4 It is this somewhat elusive concept that the Board has focused upon in evaluating the transfer of utility ownership. For greater particularity, the Board has focused on the following in order to determine if the public interest has been met in each case:

- What are the benefits and detriments to the present and potential customers, investors and shareholders of the utility being sold or transferred?
- What are the benefits and detriments to the customers, investors and shareholders of the company purchasing the utility?
- What are the benefits and detriments to the communities directly affected by the transfer?
- What are the benefits and detriments to the public interest generally?

3.1.5 In each of the past Section 26 hearings the Board has looked to these points and weighed the benefits and detriments of each factor in the transaction. The net effect on the public interest of all these benefits and detriments was then the deciding factor in recommending approval or disapproval.

3.1.6 The application of these principles to this case involves a much less complicated procedure than in past cases because the prospective owner is already fully regulated by this Board and is a half owner of the utility being purchased as well as its major customer.

3.2 RECOMMENDATIONS

- 3.2.1 One of the key issues in this hearing has been the willingness (or lack thereof) of a prospective owner to continue improvement of Tecumseh's current storage capabilities and to develop new storage.
- 3.2.2 The evidence in this and many other hearings has indicated the importance of this storage to Ontario gas users; without it, the price of gas charged to customers in Consumers' franchise area would almost certainly be higher. Consumers now takes and stores large quantities of gas during the summer which better utilizes the TCPL system and, in the end, means a higher load factor for Consumers and cheaper gas for its customers.
- 3.2.3 As well, a large provincial storage capability better insures against serious disruptions of supply caused by a major break in the pipeline in Western Canada. Such a breach in the middle of winter could have serious effects on Ontario if it were not for the ability of storage companies like Tecumseh to continue supplying gas at least in the short run.
- 3.2.4 Storage also allows the purchase of cheap spot gas purchases during the summer and permits backstopping for Consumers' customers which currently obtain their gas supplies privately and who might suffer disruption in that supply.
- 3.2.5 The ultimate test of the importance of storage is the clear evidence that without storage or significantly increased facilities, the TCPL system could not handle the seasonal requirements of the residential and high load factor non-residential customers.
- 3.2.6 The Board is acutely aware that while none of these reasons is static, each will continue to be increasingly important to the distributor's current and future customers. Continued growth in the province's natural gas market is partly dependent upon growth in its storage potential.

- 3.2.7 At present, Consumers takes delivery of about 25 percent of its annual sales volumes from Tecumseh and as such, is Tecumseh's largest customer. However, up to now it has shared control over the development and expansion of Tecumseh's storage properties with Imperial.
- 3.2.8 Tecumseh is anticipating a continued growth pattern for some years and without prejudicing this Board's duty to examine the economic feasibility of that expansion, it is obvious that Imperial's reluctance to continue any expansion of Tecumseh's currently owned assets could have a detrimental effect on Consumers' customers.
- 3.2.9 Counsel for Board Staff, Mr. Campion, argued that an examination of the public interest aspects of this application must take into account that potential storage sites will be developed whether or not Consumers owns all of Tecumseh's shares. He pointed out that it was unlikely that a potential storage site, with a proven economic value, would go undeveloped solely because Tecumseh declined to develop it.
- 3.2.10 The Board agrees with Mr. Campion that it would be difficult to imagine a set of circumstances wherein the inability of Tecumseh to purchase and develop a new storage pool would prevent that pool from being developed by another utility.
- 3.2.11 The Board is of the opinion that there is a substantial value to the public interest as represented by the owners of potential storage sites in Southwestern Ontario, of having new storage sites being developed quickly and competitively.
- 3.2.12 The Board sees a broader public interest being served to some degree if Tecumseh, under the ownership of Consumers, is active in the discovery and development of new storage areas in competition with other potential owners. In the opinion of the Board the public interest, as represented by

owners of those potential gas storage areas, also benefits to some extent from this competitiveness.

- 3.2.13 With regard to the prudence of the price which Consumers has agreed to pay for the Shares, the Board agrees with both Consumers and Board Staff that Section 26 of the Act does not require a decision as to how the purchase price should be treated for rate making purposes.
- 3.2.14 As well, the Board should not make a decision as part of this hearing in regard to inter-generational equity but nonetheless, it notes Mr. Campion's concern that Consumers is putting up a great deal of capital to ensure security of supply for future customers without the benefit of a feasibility analysis.
- 3.2.15 Both these issues must await Consumers' next rates hearing when the company will be required to justify the investment. If it is to be included in rate base, the Board's consent will be required and one of the important questions that will be decided will be the prudence of the investment. Consumers' evidence was that the costs to transfer the Shares (including the costs of this hearing) will be borne by its shareholders and no application will be made to charge them to its customers.
- 3.2.16 While the issue of the treatment accorded the purchase price for ratemaking purposes is not an issue in this hearing, its effect on the financial health of Consumers and Tecumseh is vital to the Board's recommendations to the LGIC. The Board must determine if Consumers has the financial ability to afford the purchase price without causing damage to either itself or Tecumseh.
- 3.2.17 The unchallenged evidence of Consumers' witnesses was that its debt ratings would not be affected by the purchase and because of the manner in which the transaction is structured, Tecumseh will not be affected at all. As well, the evidence showed that Consumers' capital structure will be

unchanged and that the purchase price, which represents 2 percent of Consumers' corporate assets, will have no adverse impact on the utility's financial integrity.

- 3.2.18 The Board is of the opinion therefore, that the financial strength of both companies is not adversely affected by the proposed transaction and that the public interest, insofar as the employees of Tecumseh and the shareholders and customers of Consumers are concerned, is not being compromised.
- 3.2.19 Mr. Campion pointed out that the price which Consumers negotiated with Imperial includes a premium for control and although there is a benefit to control, there is also a cost.
- 3.2.20 Counsel for Consumers, Mr. Atkinson argued that it was within the public interest for Consumers to control Tecumseh in order to avoid a deadlock on an issue concerning development of storage potential which could impact seriously on Consumers' customers.
- 3.2.21 In the Board's opinion, there is some benefit to all of Ontario if Tecumseh's owners are acutely aware of the importance of developing gas storage areas in the province.
- 3.2.22 The Board is also satisfied that, if this transaction is approved, there will be no impact on Consumers' rates at least for the 1992 test year and that any impact thereafter will require Board approval.
- 3.2.23 The normal and continued regulation of both Consumers and Tecumseh is a vital consideration in the Board's deliberations in this case and is the primary reason why the Board does not see any need for a series of undertakings as has been the case in past utility ownership transfers.

- 3.2.24 As outlined earlier, Consumers is also applying to purchase the Assets which are oil and gas related but which were held directly or indirectly by Imperial and do not comprise part of the Share purchase. Consumers must apply to the Board to purchase these Assets as a result of the Undertaking.
- 3.2.25 The purpose of the Undertaking was to ensure the continued financial integrity of Consumers by having it avoid large and potentially risky non-utility investments which could adversely affect the utility itself.
- 3.2.26 The Board agrees with Counsel to Board Staff who pointed out that the value of the non-utility assets in this case was de minimis and would have no effect on the financial integrity of the utility. However, the Assets do comprise a potential gas storage site (the Ladysmith Pool in Lambton County) which the evidence showed is an oil and gas producing reef whose oil production could be enhanced by its conversion to a storage pool because of the increased pressure from the storage operations. This could result in a public benefit to the owners of the pool and to Ontario as a whole. For these reasons the Board recommends that the LGIC approve the purchase of the Assets pursuant to the Undertaking.
- 3.2.27 Considering all the evidence and weighing the public interest factors in the manner outlined at the beginning of these Reasons, the Board is of the opinion that the purchase by Consumers of Imperial's outstanding shares in Tecumseh does not have a negative affect on the public interest and ought to be approved.
- 3.2.28 The Board therefore recommends that the LGIC approve the whole transaction as applied for by Consumers.

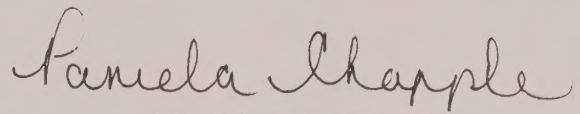
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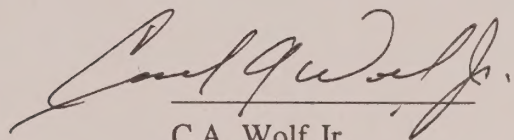
4. COSTS

- 4.0.1 The Board will issue an order in due course charging all of its costs to Consumers.

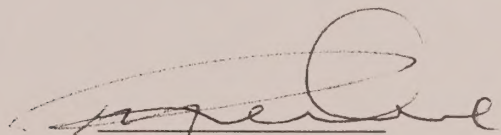
DATED AT Toronto December 10, 1991.



P.W. Chapple
Presiding Member



C.A. Wolf Jr.
Member



R.R. Perdue
Member

